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WORLD AUTOMOTIVE INDUSTRY
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WORLD AUTOMOTIVE INDUSTRY CAUSES AND EFFECTS OF THE SLUMP

Statement of the Problem

1. World vehicle production is running about 20% behind the 1973 pace. Production and sales in the United States are off by about 40%. The automotive industry, along with construction, is bearing the brunt of the general economic downswing presently affecting major non-communist economies. Vehicle producers in the United States, Western Europe, and Japan are reassessing their strategies and striving mightily to cut costs and increase their respective shares of the shrunken world market. The United States, which absorbs 40% of world automobile production, is the prime battleground.

2. The sharp decline in vehicle sales can be traced largely to the oil crisis. First came the embargo in late 1973, bringing conservation measures, queuing, and other inconveniences that discouraged potential buyers or moved them toward smaller cars. Subsequently, oil price increases boosted vehicle operating costs. Gasoline prices have shot up 60% in the United States and by similar percentages in Western Europe and Japan, where taxes traditionally have kept gasoline prices well above US levels. The increase

in petroleum prices also hurt car sales by raising auto production costs and consumer prices generally and by helping bring on the international recession.

3. Higher auto prices, traceable mainly to rising production costs, have been a major depressant on sales. US car prices have risen 15% to 25% over the past year or so. Prices were raised a half dozen times over the course of the 1974 model year, and the 1975 models were introduced with additional hikes of 8% to 10%. The average sticker price of US cars is up about \$1000 from late 1973, and the prices of imported cars have risen comparably. Recently, however, price hikes have been partially reversed by discounting and 'rebating'.

4. The general inflation is hurting auto sales by lowering real incomes across the board. Consumer prices rose an average of about 14% in the major OECD countries in 1974. Because the prices of fuel, food, and other necessities have figured prominently in the inflation, less money remains for discretionary purchases of cars and other postponable or less essential products.

5. The international recession, feeding on itself, is eroding demand for vehicles. Because of the recession, many potential car buyers have been laid off from their jobs or put on short hours and thus have been effectively

removed from the market. Other workers who fear similar fates have removed themselves from the buyers' ranks. Unemployment has not approached depression levels in the major countries, but it is rising ominously. Meanwhile, business firms that see their profits leveling off or declining are cutting back their orders for commercial vehicles.

6. The oil crisis threw a monkey wrench into the world economy at a moment when growth prospects for the highly cyclical motor vehicle industry already were worsening. Passenger car sales in the United States, including imports, had jumped 37% between 1970 and 1973 and were due to level off. World sales of motor vehicles also had shown a strong upswing. The major non-communist economies were at the top of unusually concerted business cycles in 1973, putting severe strain on capacity limits in a number of industries supplying raw and semi-processed materials. A broad growth slowdown seemed inevitable.

7. The current slump in vehicle sales is imposed on long-term trends that include serious negative factors. The number of cars relative to population and to highway networks seems to be approaching practical limits in many countries. There already is one car for every 1.8 people in the United States, or an average of about two cars per family. Australia and Canada are not far behind. The

countries of the European Community, Sweden, and Norway have one car for every three or four people, or an average of about one per family. Traffic congestion clearly is a constraint in the United States but probably is more of a limiting factor in Italy, the United Kingdom, West Germany, and the Netherlands. All of these countries have about 70 vehicles per mile of roads versus only about 30 in the United States. The greater population density of Europe at once limits the potential for relieving congestion by building more roads and renders public transportation a more practical alternative. Japan's auto industry faces a concentration of vehicles and people in the country's Pacific Industrial Belt that must be very discouraging.

8. The slowdown in population growth is another factor working to retard automobile sales over the longer term. In the biggest market, the United States, population growth has slowed progressively since the 1950s and now is less than 1% per year. Population growth also has slowed in the European Community and is projected at 0.5% per year. Japan's population growth has been stable for some time at about 1% per year.

9. Producers in Western Europe, Japan, and the United States see only limited opportunities for exporting to

countries outside their own ranks. The incomes of the least developed countries will not support large car purchases for many years to come. More advanced countries -- Spain, South Africa, Australia, and the larger Latin American countries -- are encouraging and protecting automobile production on their own soil and offer limited opportunities to manufacturers in other countries. Argentina, to cite an extreme example, imported only 376 vehicles in 1972. Spain and Brazil even hope to become important exporters of vehicle in the near future. Canada enjoys free trade in automobiles with the United States and has a sizable industry. The principal oil exporting countries are importing more vehicles this year, but aside from Iran and Venezuela their auto markets are small either because their populations are small or because development needs take precedence. These countries probably will follow Iran's lead and insist on local manufacture as their demand for vehicles increases.

10. Auto producers delayed the full impact of the slump for some months by permitting inventories of finished vehicles to build up. Manufacturers in Germany, Japan, and other countries pushed exports to the United States in the face of weakening sales until storage lots were parked full as far inland as Denver. By mid-summer 1974, the backlog of imported cars was estimated as high as 600,000

units, the equivalent of five months' sales. At the end of the year, most foreign manufacturers still were struggling with oversized inventories and slow sales at home and in the United States. While inventories of US cars rose as high as 1.2 million units, the backlog of 1974 models was worked off in early autumn by publicizing the sharp price increases being imposed on 1975 models. The 1975 models, however, sold very slowly and inventories accumulated until production cutbacks and price rebates brought relief.

11. The drop in auto production inevitably has impacted on a number of industries -- steel, non-ferrous metals, rubber, glass, and so forth -- that supply the auto industry. Similarly, reduced consumer spending by people laid off from or put on short time in the automotive and related industries is broadening the slowdown in economic activity.

12. In early 1974, the US auto industry had 113,000 workers on indefinite layoff, and at least 115,000 more were laid off temporarily during the first nine months of the year. Layoffs probably hit a peak in mid-winter. Workers have been laid off for short, pre-specified periods in a number of cases both in the United States and abroad. Outside the United States, Germany was among the first to resort to intermittent layoffs, and Volkswagen has used this tactic

repeatedly. Many auto makers have trimmed workweeks, and overtime work has disappeared for most of the people still employed. Cutting the workweek is the usual tactic in countries such as Japan and Italy, where customs and legal restrictions militate against outright layoffs. In Italy, 71,000 Fiat workers went to a 26-hour workweek last fall.

13. The impact of declining vehicle sales on world trade flows was not great until the second half of 1974. Last year's spurt in US demand for small cars and subsequent inventory building postponed the trade drop. It now appears that the value of US vehicle imports will level off near the 1973 level of \$7 billion. Sales of imported vehicles are running about 20% behind the 1973 pace in terms of units, but prices have risen by an offsetting amount. This leveling will help the United States contain the trade deficit resulting from the recent quantum jump in oil prices. Conversely, it will weaken the trade balances of exporting countries, which except for West Germany and Japan are experiencing serious deficits. Again, it must be emphasized that the exporters have no suitable alternative to the US market, which still absorbs about two-thirds of world automobile imports.

Response to the Problem

14. Automotive companies around the world have adopted a number of policies and tactics to reverse the profit decline. Individual companies typically are moving on several fronts simultaneously.

15. All producers have adjusted prices.

- The US companies and most foreign firms boosted prices, hoping that the negative effect on sales volume would be minor. When sales continued to plummet, they resorted to discounting and rebating.
- US firms slapped the biggest percentage increases on the smaller models.

16. Product mixes have been altered in favor of smaller models.

- US companies have introduced a number of new models in the compact and subcompact fields -- some of them luxuriously appointed* -- and are devoting a greater portion of their production to the smaller cars.
- Foreign firms, already concentrated at the smaller end of the model range, are emphasizing still smaller vehicles and luxury compacts.

*According to Lee A. Iacocca, President of Ford Motor Company, "People want economy, and they will pay any price to get it."

17. Producers are striving to improve their vehicles technologically.

- Honda is manufacturing and licensing others to manufacture the CVCC (compound vortex controlled combustion) engine, which satisfies US emission standards without a catalytic converter and is economical on fuel.
- Yamaha claims to have developed an automobile engine that has the virtues of the CVCC engine and will cost less to build.
- Volkswagen has introduced new compact and subcompact models that are far more sophisticated than traditional Volkswagens.
- Electronic ignition systems are being used to reduce operating costs.
- Automotive engineers are making strenuous efforts to improve fuel economy.

18. Extensive cost reduction efforts are underway.

- Chrysler Corporation began a broad cost-cutting program after having reduced its work force 8% from 1973 levels; the program has involved administrative streamlining, dismissal of a large number of salaried employees, and reduced investment.

- Ford also has begun a broad cost reduction program, and General Motors may follow.
- Volkswagen has reduced its payroll by 10,000 workers, or 8%, and is offering bonuses ranging up to \$3,400 for further resignations or early retirements.
- Opel also offers bonuses to encourage resignations.

19. Various automotive firms are consolidating to cut costs and reduce competition.

- Peugeot has acquired Citroen's automobile operation while Renault has picked up Berliet, Citroen's truck subsidiary.
- Volvo boosted its interest in the Dutch auto firm DAF to a majority position last September.
- Fiat recently took control of Klockner-Humboldt-Deutz, a truck producer, and made an arrangement with Alfa Romeo and Saviem for joint production of diesel engines.

20. Some companies will build or expand plants in other countries to take advantage of lower costs or protected markets.

- Volvo is building a plant at Chesapeake, Virginia, that is to come on stream in 1976.

- Fiat is building a big plant in Brazil.
- Ford is assembling simple vehicles in the Philippines and Thailand, and General Motors has a similar program in Malaysia.

21. Product diversification is the strategy of several companies.

- American Motors has begun to build buses and light commercial vehicles.
- Volvo has entered the sporting goods industry.
- Saab-Scania has formed a subsidiary to sell computers in the United States.
- Renault has bought into a bicycle and motorbike company and plans to produce equipment for uranium enrichment and pollution control.
- Fiat intends to become a major builder of schools, hospitals, and industrial buildings.

22. Various types of government assistance will be given to ailing firms. Some companies, notably Renault and Alfa Romeo, already are government-owned and should have little difficulty obtaining financial support to carry them through difficult times. London is bailing out British Leyland and taking an equity stake in the firm. Some outright

nationalizations could occur. Japanese firms can obtain financing on favorable terms from the Long-Term Credit Bank of Japan and probably can count on direct government assistance in an emergency. Increased protection against imports may be granted anywhere that domestic producers are in a slump and imports are significant. Last year the United Auto Workers Union lobbied unsuccessfully for quotas on vehicle imports into the United States. More recently, Australia has cut vehicle imports by applying strict quotas. European governments may move to limit imports from Japan, the main source of competition from outside the continent.

Prospects

23. Automotive output will recover slowly in the major producing countries. Weak real aggregate demand will continue to depress sales of passenger cars and commercial vehicles. Car sales will recover even slower than aggregate demand, however, because cars are big ticket items whose purchase usually is deferrable and because recent price increases on vehicles and motor fuel have been very steep.

24. Smaller cars that economize on fuel will be popular unless the price spread between large and small cars is kept narrow. The less luxurious and therefore less expensive models should sell best until personal incomes regain lost ground.

25. While automakers will keep trying to revive profits, some will not succeed and will go out of business, be merged into other firms, or be bailed out by government assistance. The scramble for export markets will go on, as will cost-cutting and the drive for product innovations. Investment plans will be scaled down, but production will be expanded in favorable -- often protected -- locations. Exchange rate adjustments may weaken the US competitive position; if not, foreign companies will continue to move toward production in the United States.

26. Personal incomes will slowly catch up with automobile prices. The prices of raw materials generally have weakened in recent months, and auto workers' unions should put less push on prices as long as many of their members are idle or working short time. However, in the United States and elsewhere, auto workers' wage rates are tied formally or informally to consumer prices.

27. Although sales of foreign cars in the United States have been strong in recent months, the competitive position of US producers seems better than it was before the 1971 currency adjustments. Unit labor costs now are about as high in West Germany or Sweden as in the United States, and the gap between US unit labor costs and those of Japan and other

countries has narrowed appreciably. Materials costs also seem to have moved in favor of US producers. Steel in particular is available in the United States at more competitive prices.

28. The US companies should be able to maintain or improve their present share of the American market even though foreign firms are well established in the important small car sector. US producers will not, however, be able to score any sizable increase in exports.

UNITED KINGDOM AUTOMOTIVE STATISTICS

Year	Output	Registrations	Exports	Imports	Net Exports	Change in Inventory	Cumulative Inventory*	Inventory At Current Selling Rate*
973								
January	238,691	120,588	74,302	38,999	35,303	82,800		
February	171,087	150,569	60,260	28,139	32,121	-11,603		
March	191,898	183,443	60,316	33,002	27,314	-18,859		
April	156,262	148,521	56,658	31,544	25,114	-17,373		
May	213,649	128,990	75,703	32,933	42,770	41,889		
June	185,470	129,000	63,368	34,284	29,084	27,396		
July	127,545	149,850	45,385	30,274	15,111	-37,416		
August	141,684	149,850	50,710	30,531	20,179	-28,345		
September	172,726	129,000	62,249	36,917	25,332	18,394	18,394	2
October	166,598	127,000	72,103	29,523	42,580	-2,982	15,412	2
November	185,894	126,000	68,309	34,738	33,571	26,323	41,735	5
December	199,587	103,000	74,787	30,568	44,219	52,368	94,102	13
974								
January	105,305	113,000	60,518	30,580	16,643	-4,338	89,765	16
February	139,995	109,000	62,149	30,000	32,149	-1,154	88,611	12
March	164,069	106,000	57,873	30,000	17,873	40,196	128,807	21
April	115,328	98,000	52,188	25,000	15,917	1,411	130,218	24
May	155,550	149,428	62,705	25,000	37,705	-31,583	98,635	12
June	140,000	117,000	73,211	25,000	48,211	-25,211	73,424	9
July	131,600	105,000	68,972	25,000	43,972	-17,372	56,052	0
August	150,000	127,495						
September	150,605	114,997						

Since September 1973

WEST GERMAN AUTOMOTIVE STATISTICS

Year	Output	Registrations	Net Exports	Change in Inventory	Cumulative Inventory*	Inventory At Current Selling Rate*
1973						
January	361,322	184,989	126,557	49,776		
February	355,783	210,779	135,425	9,579		
March	393,854	280,838	125,886	-12,870		
April	339,143	259,631	153,137	-73,625		
May	389,438	241,966	120,737	26,735		
June	332,813	219,513	115,663	-2,303		
July	217,949	187,291	89,952	-59,294		
August	248,341	132,401	120,006	-4,066		
September	341,597	153,132	139,241	49,224	49,224	4
October	379,622	174,676	188,439	16,507	65,731	4
November	362,189	134,793	141,498	85,898	151,629	14
December	225,760	80,003	120,100	25,657	177,286	23
1974						
January	309,260	117,525	156,402	35,333	212,619	20
February	285,092	138,043	176,796	-29,747	182,872	13
March	315,616	203,889	184,921	-73,195	109,677	7
April	285,165	213,580	173,743	-102,158	7,519	0.5
May	311,678	210,632	132,328	-87,163	-79,644	-4
June	216,378	210,000	84,130	-77,752	-157,416	-11
July	201,211	200,000	78,746	-77,535	-234,951	-19
August	179,226	190,000	111,108	-21,962	-256,913	-28

*Since September 1973

JAPANESE AUTOMOTIVE STATISTICS

Year	Output	Registrations	Exports	Change in Inventory	Cumulative Inventory*	Inventory At Current Selling Rate*
1973						
January	503,222	244,400	164,227	94,595		
February	576,933	362,412	166,897	47,624		
March	631,366	375,000	174,929	81,437		
April	560,444	365,000	168,836	26,608		
May	610,081	358,470	191,303	60,308		
June	644,279	333,000	162,211	149,068		
July	596,124	390,914	195,808	9,400		
August	517,630	325,000	158,331	34,299		
September	609,173	300,000	162,928	218,605	218,605	11
October	644,389	275,000	170,784	198,605	417,210	25
November	626,197	250,000	179,721	196,476	613,686	37
December	562,919	200,000	217,222	145,697	759,383	47
1974						
January	514,844	198,208	169,991	146,645	906,028	63
February	553,270	194,253	199,815	159,202	1,065,230	64
March	584,950	225,000	219,384	140,566	1,205,796	70
April	501,104	230,000	210,000	61,104	1,266,900	74
May	533,089	243,531	210,000	79,558	1,346,458	80
June	520,141	311,168	210,000	-1,027	1,345,431	65
July	566,474	270,400	178,860	117,214	1,462,645	75
August	433,534	207,811	179,720	46,003	1,508,648	86
September	587,005	296,133	222,124	68,748	1,577,396	64
October		311,828				

*Since September 1973

FRENCH AUTOMOTIVE STATISTICS

Year	Output	Registrations (Autos Only)	Exports	Imports	Net Exports	Change in Inventory	Cumulative Inventory*	Inventory At Current Selling Rate*
1973								
January	328,895	169,153	127,417	31,221	96,196	63,546		
February	308,340	169,170	128,276	44,561	83,715	55,455		
March	346,818	186,476	135,070	47,737	87,333	73,009		
April	226,272	192,813	122,065	36,507	85,558	-52,099		
May	344,248	182,022	118,770	53,688	65,082	97,144		
June	333,862	163,446	134,864	51,867	82,997	87,419		
July	327,205	153,508	132,680	36,718	95,962	77,735		
August	53,061	131,579	24,850	32,061	-7,211	-71,307		
September	315,412	162,909	132,168	39,921	92,247	60,256	60,256	5
October	375,626	162,900	127,927	49,101	78,826	133,891	194,147	18
November	343,640	158,480	125,219	55,327	69,892	155,268	309,415	28
December	287,927	154,050	102,338	44,456	57,882	75,995	385,410	39
1974								
January	346,891	149,764	120,956	46,008	74,984	122,143	507,553	48
February	306,950	127,805	139,907	40,844	99,063	80,002	587,555	52
March	322,422	149,000	164,728	42,575	122,153	51,269	635,824	52
April	327,272	178,284	189,150	50,060	139,090	9,898	648,722	45
May	322,375	181,309	193,691	45,000	148,691	-7,625	641,097	46
June	293,066	129,538	218,761	28,540	190,221	-26,293	614,404	38
July	307,266	160,404	210,621	27,926	182,695	-35,833	578,571	35
August	419,162	148,065	33,699					
September	251,996	106,915	139,715					

*Since September 1973

UNITED STATES AUTOMOTIVE STATISTICS

Year	Output	Registrations	Imports	Change in Inventory	Cumulative Inventory*	Inventory At Current Selling Rate*
1973						
January	792,275	880,000	160,000	72,275		
February	1,077,759	918,100	155,000	314,659		
March	936,120	1,141,195	157,000	-48,075		
April	843,242	1,200,000	159,000	-197,758		
May	940,400	1,115,304	174,000	-30,905		
June	922,444	1,081,485	173,000	13,959		
July	705,952	817,906	150,000	-101,954		
August	727,448	835,000	143,000	35,448		
September	1,065,428	875,400	136,154	326,182	326,182	9
October	1,176,286	876,070	138,508	338,724	664,906	18
November	1,287,144	888,000	157,157	536,301	1,201,207	34
December	801,073	890,730	117,000	327,343	1,528,550	67
1974						
January	634,313	678,000	125,500	81,813	1,610,363	61
February	606,479	682,000	115,000	39,479	1,649,842	58
March	591,874	779,000	114,600	-72,526	1,577,316	52
April	677,783	815,000	113,000	-24,217	1,553,099	49
May	729,857	880,000	115,000	-35,143	1,517,956	46
June	660,105	811,000	113,000	-37,895	1,480,061	45
July	747,051	807,904	117,000	56,147	1,536,208	42
August	720,000	809,000	127,380	38,380	1,574,588	43
September	667,944	727,884	132,000	72,060	1,646,648	45
October		756,100	123,600			

*Since September 1973

MOTOR VEHICLE PRODUCTION (000)

	<u>FRANCE</u>	<u>WEST GERMANY</u>	<u>ITALY</u>	<u>UNITED KINGDOM</u>	<u>JAPAN</u>	<u>UNITED STATES</u>
1965	1641.7	2976.5	1175.5	2177.3	1875.6	11137.8
1966	2024.6	3050.7	1365.9	2042.4	2286.4	10396.3
1967	2009.7	2482.3	1542.7	1937.1	3146.5	9023.7
1968	2075.6	3107.0	1660.4	2225.1	4085.8	10820.4
1969	2459.1	3604.6	1596.0	2182.8	4674.9	10205.9
1970	2750.1	3842.2	1854.3	2098.5	5289.2	8283.9
1971	3010.3	3982.7	1817.0	2198.1	5810.8	10671.7
1972	3327.6	3818.4	1840.2	2329.2	6298.8	11268.0
1973	3596.4	3954.0	1959.8	2163.6	6978.0	12636.0
1974	3461.6	3070.0	1770.0	1933.0	6560.0	7111.0

EMPLOYMENT IN US AUTO INDUSTRY

	<u>Current</u>	<u>Year Ago</u>	<u>Change</u>	<u>Peak layoff (March 74)</u>
GENERAL MOTORS	376,000	449,000	-73,000	-84,000
CHRYSLER	114,000	124,000	-10,000	-16,500
FORD	181,000	181,600	-600	-12,600
AMERICAN MOTORS	23,800	21,200	+2600	0